



Bernard A. Streeter
Mayor
City of Nashua



MEMORANDUM

Date: July 23, 2002

To: Board of Aldermen

From: Bernard A. Streeter, Mayor

Re: Status of proposed merger of Pennichuck Corporation with Philadelphia Suburban Corporation

The NH Public Utilities Commission (PUC) granted the request by the City of Nashua for full intervener status in the above proceedings as a result of a pre-hearing meeting we attended on Friday, July 19th. Intervener status was also granted to a number of neighboring communities, organizations and citizens. Intervener status provides for participation, input, notice and all reports of proceedings.

The schedule as proposed by the PUC (attached) is two months shorter than the minimum the City proposed at Friday's meeting. Therefore, the timeframe that the Board of Aldermen need to reach some decisions on the future direction of our drinking water supply will be very constrained.

As you can see on the PUC's schedule, final responses from Pennichuck Corporation to data requests by the City may not be received until Sept. 27th. All of these responses are necessary for the consultants' analysis. Therefore, I anticipate submitting the **draft report** from our consultants to the Board of Aldermen in the form of a **Resolution** at your **October 22nd** meeting. Testimony offered by the City to the PUC is scheduled for **Dec. 10th**, and needs to reflect the Board's position. Therefore a vote on this by **November 26th** will be appreciated.

I realize the short timeframe we will be working within and I will do everything within my power to assure timely information and opportunities for public input.

Information will be provided to you and the citizens of Nashua as we receive it via Nashua's web site, www.gonashua.com, and hard copies at the library, the City Clerk's office and the Aldermanic Office.

The PUC will be scheduling several public hearings to receive input from Nashua's citizens and those of our surrounding communities. The PUC's Technical Committee is determining the feasibility of a workshop in early October to discuss the financial perspective of water utilities.

I have also requested several dates be set-aside on the Aldermanic calendar to allow sufficient discussion and public input once the draft report is received by the Board of Aldermen and the legislation is introduced.

I welcome any other ideas you might have to assure that we make the best decisions for Nashua's future on this critical issue within the tight timeframe proposed by the PUC.

Below is the most recent Telegraph article on the proposed merger:

Tuesday, July 23, 2002

Pennichuck merger schedule lengthened

By BRAD LEIGHTON, Telegraph Staff
leightonb@telegraph-nh.com

PENNICHUCK TIMETABLE

NASHUA – The timeline for the proposed acquisition of Pennichuck Corp. has lengthened, which may prove beneficial to the company's shareholders and its communities, said Maurice Arel, the company's president and chief executive officer.

"The procedural schedule set by the PUC brings it out to the beginning of next year, which delays the whole process," Arel said. "Right now we are in a wait-and-see game."

Pennichuck had proposed a schedule that would have been about a month faster, and the city would have liked a slower schedule, Arel said. The PUC considered both and came up with a tentative schedule that would see a decision on the merger on Feb. 28.

The tentative schedule has Nashua, the towns and other interveners giving testimony on Dec. 10.

The "drop-dead date" written into the acquisition deal is March 31, Arel said, so a decision would have to be reached before then. The company originally wanted a decision by Sept. 30, but Arel said the PUC schedule is acceptable.

"It may turn out for the best for all parties involved," he said.

That delay will give the communities more time to gather information about the deal and about Pennichuck's suitor, Pennsylvania-based Philadelphia Suburban Corp., Arel said.

Arel is confident that as people learn more about Philadelphia Suburban they will feel better about the merger.

The extra time will also give Philadelphia Suburban's stock price a chance to recover.

The company's stock has taken a double whammy in the last few months. It has suffered because of poor weather conditions in its main markets, Pennsylvania and New Jersey, and from news that its largest single investor, Paris-based Vivendi Environnement, plans to divest its 16 percent share in the company.

The acquisition is a stock-for-stock agreement based on Philadelphia Suburban's stock price. That price has fallen 30 percent since the Pennichuck deal was struck, and the local utility's stockholders have expressed concern about the value of the agreement.

"The one negative of the Pennichuck agreement is that our stock is down," said Nicholas DeBenedictis, the chairman and president of Philadelphia Suburban. "I have to be honest and say that Pennichuck's shareholders are less happy now than when the agreement was first announced."

"We are hoping that by the time the regulatory approval process is done, our stock will have recovered."

DeBenedictis was confident that the merger would pass the regulatory hurdle. "We have to show that there will be no net harm caused by the merger. We think we can show that, not only that there would not net harm, but in fact it will be a benefit."

Pennichuck directors will discuss the merger during their regularly scheduled meeting on Aug. 2. The prospectus on the agreement has not yet been completed and a date for the shareholders' vote has not been set, Arel said.

Both Pennichuck and Philadelphia Suburban officials said they have been in regular contact with each other.

Philadelphia Suburban hopes the Vivendi situation will be resolved through a secondary public offering of Vivendi's 11.1 million shares. Philadelphia Suburban's executives have hit the road to sell the second offering to its other investors in hopes they will help absorb the majority of the stock.

The company could buy back about 2.5 million of its own shares, but company officials are hopeful the secondary offering will be oversubscribed.

Philadelphia Suburban's second quarter earnings, released Monday, were just about what was expected, said David Schanzer, a water utility analyst with Janney Montgomery Scott.

The company reported net income of \$14.8 million for the quarter, or 21 cents per share, compared with \$15.4 million in last year's second quarter. Revenue fell to \$76.6 million in the quarter from \$77.2 million last year because of a wet June – when people didn't choose to water their lawns – and drought restrictions in Pennsylvania and New Jersey in July. Both states have since eased their drought restrictions.

After Vivendi announced in May that it was divesting its interest in Philadelphia Suburban, the utility's stock prices have fallen 30 percent. Many analysts, including Schanzer, now argue that the stock is undervalued.

"They don't deserve to be down there at \$16 and change and I'm betting that after the Vivendi situation is resolved, they won't be," Schanzer said.

The Vivendi divestiture decision was driven by the need to pay off its own heavy debt and had nothing to do with Philadelphia Suburban's performance, Schanzer said.

Similarly, the weather is out of the utility's hands, although the company has become more geographically diverse through acquisitions. That has allowed it to weather Mother Nature better – a drought in Pennsylvania can now be offset by more favorable weather in Ohio or North Carolina.

"I think Pennichuck investors will realize that the company will be better under Philadelphia Suburban's umbrella," Schanzer said.

Pennichuck, which will retain its local leadership and keep its name under the merger, will save money on materials such as piping and will be able to borrow at a lower interest rate and take advantage of Philadelphia's more advanced technical labs should the merger be completed, company officials have said.

"I've visited Pennichuck and they've got a good management team, so I'm not saying they wouldn't do all right if the merger didn't go through. What I'm saying is that they'd do even better as part of Philadelphia Suburban," Schanzer said. "It's pretty much universally agreed that Philadelphia Suburban's management does a good job."

However, the stock market's overall woes have reached down to even the safest stocks, Schanzer said. Water utility stocks are considered safe because the regulatory process ensures a fair return on investment. Philadelphia Suburban has averaged a 9 percent annual growth rate over the last five years.

"People are even selling off the utilities. I think it is because they don't have anything else to sell now. It seems more emotional than anything now. You know how Roosevelt said 'All we have to fear is fear itself.' Well, this is the fear."

Philadelphia Suburban's stock avoided the market malaise with shares popping up to \$16.70 on Monday – a 42-cent increase over Friday's close of \$16.28.

The upswing had less to do with its earnings report than it did with a positive article on Monday in the Wall Street Journal, Schanzer said.

The article quoted several analysts who said the stock was undervalued.

Pennichuck, which had revenues of \$22.7 million in 2001 compared to Philadelphia Suburban's \$307.3 million, hasn't enjoyed the same national exposure.

Pennichuck's stock slipped by 76 cents – a little more than 3 percent – to \$24.24 by the close of business on Monday.

PENNICHUCK TIMETABLE

The following is a the tentative schedule proposed by the state Public Utilities Commission for the proposed acquisition of Pennichuck Corp. by Philadelphia Suburban Corp.

Aug. 2 – PUC staff requests information.

Aug. 16 – Pennichuck and Philadelphia Suburban respond.

Aug. 21 – Technical session.

Aug. 23 – PUC requests more information.

Sept. 6 – The companies respond.

Sept. 13 – More information requested by PUC.

Sept. 27 – The companies respond again.

Oct. 10 – Technical session.

Oct. 24 – Companies respond to the technical session.

10 – Testimony from interveners and PUC staff.

Dec. 20 – PUC staff requests more information.

3 – The companies respond to request.

Jan. 8 – Technical session.

Jan. 22 – Rebuttal testimony.

Jan. 29 – Additional information requested.

Feb. 5 – Information received.

Feb. 17 to Feb. 19 – hearings.

Feb. 28 – Order issued.

cc: Special Pennichuck/Suburban Study Committee